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As competition intensifies in the retail financial services marketplace, accurate measures of customer value down to the account level are becoming increasingly pivotal to success at the retail end of the market. This applies both to established players and new entrants.

CUSTOMER VALUE: GAINING THE COMPETITIVE EDGE

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The fact is that the pressures that have made profitability measures a prerequisite in the corporate marketplace are now increasingly present in the retail sector. Individual consumers are becoming ever more demanding, both on price and service. At the same time, institutions are looking to gain a competitive edge by establishing one-to-one relationships with customers and a higher degree of personalisation in their services. Significantly, the one factor which had previously hampered the application of profitability measures to individual accounts — the sheer volumes of data involved — has been addressed by advances in technology.

New technology, new insight

While the concept of establishing customer profitability is being imported from the corporate market, the systems to handle the measurement are not. Traditionally, banks used to measure customer value by building bespoke systems, generally developed in-house on the mainframe. This would be a massive application, pulling in data from a whole range of operational systems. As customers, circumstances and requirements changed, these applications became increasingly complex, due to the original design being overlaid with a rolling series of piecemeal changes.

The underlying problem with these mainframe-based approaches to measuring retail customer profitability was that it is a dynamic, fast-changing and fluid area where flexibility is key. This is especially true given that measurement must be conducted right down to the account level if the real benefits are to be realised. Experience has shown that the 'half-way house' approach of analysing profitability on the basis of sample accounts or high-level averages, or only down to the level of branches or products, is too limited and rigid to deliver the degree of flexibility, responsiveness and functionality now required.

In contrast, by establishing the value of each account to its business, the institution gets all the benefits of detailed data, plus the ability to aggregate this data in an infinite variety of ways. The value of this capability is reflected by the wide range of functions across the institution which queue up to make use of aggregated account data as soon as it becomes available. In fact, our experience with financial services institutions worldwide — who have adopted NCR's Value Analyzer solution to drill down to account-level profitability information — shows that virtually every department benefits directly.

Direct benefits across the organisation

The most immediate advantages arise in marketing and customer management. For any marketing initiative, it is crucial to understand what products are important and attractive to which customers, and which customer groups are likely to use a product in a way that is profitable to the provider. With products such as banking current accounts, where profitability is determined by customer behaviour, account-level information may be decisive in determining both the target market and the pricing.

Customer retention and incentivisation can be similarly transformed by the detailed data on customer profitability. Using the information to focus on profitable customers, in a way which matches their behaviour, can result in substantial savings on the retention budget — while also delivering better bottom-line results for the institution in the long-term. Incentives to encourage customers to stay, or to move to new products, can also be applied more effectively and efficiently.

Everywhere you look, the benefits are equally

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dramatic. For example, the profitability of various channels can be notoriously difficult to ascertain accurately. But the profitability of individuals using a particular ATM could be established very easily, aiding any decision on whether that equipment was worth retaining or even upgrading. Similarly, the data might indicate that a particular product is being used by a large number of customers in a very unprofitable way. This situation might be addressed — and the profitability of the product improved — either by redesigning the product, or by incentivising customers to use it more appropriately.

Looking forward, the benefits are likely to increase still further. Relationship pricing — one of the original drivers behind customer profitability measures in the corporate banking sector — is beginning to emerge as a key aspiration for retail financial services providers. Now retail customer value data opens the way for it to become a reality. As banks move to a customer-focused basis for their organisational structure, dynamically generated customer profitability figures can form the ideal basis for defining the scope of each business unit. And in sales and service, a customer value system can provide an objective and ongoing basis for allocating staff rewards and defining 'banded' customer service levels.

Moving to customer value systems

Given the potential effects across the business, it is hardly surprising that the move towards account-level customer profitability measurement is accelerating rapidly — and institutions that hang back are clearly risking being left behind. NCR's experience among its own global financial services clients demonstrates the speed with which the benefits can flow through, and their applicability to institutions at each stage of development.

For example, NCR recently advised a major new UK-based entrant to the banking sector, which was taking on massive numbers of new accounts at a very rapid rate. These circumstances made it crucial for the bank to establish the profitability of these accounts at the earliest possible stage, in order to meet its business plan and justify its business model. Customer value analysis provided the answer. At the same time, moving straight to customer value analysis enabled this new player to leap-frog an entire stage of development and experience, giving it the tools needed to make informed decisions without first having to build up years of retail banking knowledge.

At the other end of the scale, the well-established Royal Bank of Canada recently conducted an exercise that demonstrated the improved accuracy available from measuring profit at the account level and using this as input into customer segmentation. The bank took a sample set of clients and measured their value using an in-house product profitability model comparable to NCR's account-based profitability model (aggregated to the customer level). The result was that 75 per cent of clients moved two or more deciles — with the result that the bank redirected its marketing efforts towards the redefined segments that reflected the behavioural-based calculations of NCR's Value Analyzer.

Another NCR customer, a UK high-street bank, developed its own tactical customer value application and wanted to move to a sustainable strategic platform. The potential problems of maintainability over time with such a system meant it decided to combine its existing learnings with the flexibility and adaptability of NCR's Value Analyzer. The result was a system able to handle the dynamic nature of retail customer value analysis (and this in turn will enable the bank to take on new types of products, and also to respond to new product portfolios arising through acquisition or organic growth.

Conclusion: the organisational challenge

From such examples, it is clear that financial institutions are now seizing the opportunities presented by customer value systems. Interestingly, the fact that the application and demonstrable benefits of the data are so widespread across the business means the initial challenges in making the move may appear to be organisational rather than technological. Getting all the different areas of a bank to agree on precisely how the data should be collected and used can be difficult.

However, such disagreements are actually illusory. By capturing the smallest possible item of data, and combining it with the capability to aggregate and analyse it in an infinite variety of different ways, a customer value system brings the flexibility to give everyone in the organisation precisely what they want. Which means the organisation as a whole gets the real commercial benefits that it — and its shareholders — require. >

Biography

Simon Doherty, a career banker and a qualified accountant, joined NCR's Financial Solutions Group in 1997 to work in their data warehousing area, focusing on financial services organisations. Simon is currently responsible for NCR's customer value practice in the UK and the Nordic Region. In this role he has been closely involved in the development of the corporation's global customer value solution 'Value Analyzer™' and its promotion and implementation in a number of major retail banks. Prior to this, Simon worked in the financial and management information area of NatWest between 1986 and 1997. He was involved in management information projects in various parts of the NatWest Group including the UK retail, corporate and international divisions, Lombard North Central, Ulster Bank and Coutts.

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